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## **Asia's economic growth: trends and patterns**

Sudha Venu Menon

ICFAI Business School, Ahmedabad

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## ASIA'S ECONOMIC GROWTH: TRENDS AND PATTERNS

*SUDHA MENON*

The spectacular growth of economies in Asia over the past few years has amazed the economics profession and has evoked a torrent of books and articles attempting to explain the phenomenon. Since 1960 Asia, the largest and most populous of the continents has become richer faster than any other region of the world. Asian growth, like that of the Soviet Union in its high-growth era, seems to be driven by extraordinary growth in inputs like labor and capital rather than by gains in efficiency. Of course, this growth has not occurred at the same pace all over the continent. The eastern countries turned in a superior performance, although variations in achievement can be observed here too. This impressive achievement is, however, still modest compared with the phenomenal growth of Developed countries in the west. Strong Total Factor Productivity [TFP] rapid accumulation of physical and Human Capital and trade policy coupled with effective policy intervention played vital role in Asia's spectacular success. Naturally, sustainable growth performance and elimination of poverty demand greater role of institutional reforms industrial development and macro economic stability.

### ASIAN ECONOMIC PERFORMANCE-AN OVERVIEW

It is widely accepted in academic and intellectual discussion that the rise of Asia during the last few decades has significantly reduced its gap with USA; especially in term of income percapita in other advanced economies. While Latin American and African countries failed to achieve this spectacular growth, Asia's real income percapita increased sevenfold within the last five decades<sup>1</sup>. Economic performance of Asian countries differs across regions and countries, because there exists wide gap in the period of growth take off actually started. For example, Japan initiated economic integration early in 1955, while other Asian countries opened up their economy only in 1990s. Newly Industrialized Economies [NIEs]<sup>2</sup>, ASEAN<sup>3</sup>, China and India initiated integration process in 1967, 1973, 1979 and 1982 respectively. Even though the later developers started their take off at lower income levels than Japan and NIEs, the overall pace of performance is not significantly different from Japan and NIEs at respective stages of growth. So it is evident that *integration with world economy and free trade policies* made a tremendous impact on Asian Success. During the period between 1970-2005, Asia's share in world trade raised double times where as Latin America's share declined. But in terms of participation in world trade also we can see inter regional variation. Even though China started late with lower base, now it is ahead of other countries in terms of global trade<sup>4</sup>.

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<sup>1</sup> World Economic Outlook, IMF, 2006.

<sup>2</sup> NIEs include Hongkong, Singapore, Korea and Taiwan

<sup>3</sup> Indonesia, Malaysia, Philippines and Thailand.

<sup>4</sup> Rapid Growth of selected Asian Economies: India and China, Policy assistance series, FAO regional Office, 2006.

Another factor, which plays pivotal role in Asian success, is *declining dependency ratio*. Dependency ratio implies ratio between non-working age population and total population. Here also the regional diversity is striking. While significant progress has been made in economic growth, the effect of this double digit growth is not distributed equally among population. Indeed almost 700 million Asians or 20% of the total population still lives in extreme poverty. Thus, Sustainability of the growth process in Asia is closely linked to the effective eradication of rural poverty<sup>5</sup>.

As mentioned above, demographic transition, labour mobility from low to high productivity sectors, factor accumulation within sector and technological progress are main elements of Asian success. To analyze these factors and extent of sustainability, we have to explore sectoral analysis of growth.

While we link output per capita with changes in labor productivity, participation rates and age structure of the population, it is clear that during 1975-2005, growth across the region is driven mainly by labor productivity. While we decompose, growth in labor productivity into increase in physical capital per worker rising labor quality and growing TFP, the result shows that during the same period Asia witnessed faster physical capital accumulation and faster TFP growth than other developing countries<sup>6</sup>. Development in education also played pivotal role, making the growth on average by ½ percentage point. Here also the inter regional variation in development and growth potential is significant, making policy environment and intervention accordingly.

TFP contributed 0.75 to 2 % growth point in India Japan, NIEs and Thailand. In Japan, TFP growth declined steadily after take off. In ASEAN 4 low average TFP growth masks significant cross country heterogeneity. Eventhough China started late; its performance in TFP is well ahead of other countries in the region.

In the globalization era, IT sector growth and knowledge dissemination play vital role in overall economic growth. The IMF study of 2006 indicates that economy wide investment in ICT capital had impact on growth averaging about ½ percentage points in the NIEs and China. But here, non ICT capital impact is high in Asia compared to developed economies.<sup>7</sup>

## SECTORAL IMPACT ASSESSMENT

As mentioned earlier, sectoral mobility effect from low to high productivity sectors resulted in high growth rate in Asia. Here we should be clear that sectoral shift is not a mechanical process and their speed and extent reflect the willingness and ability of labor and capital to move towards higher productivity uses. Policy intervention matters here also. This article attempts to analyze sectoral implications taking agriculture, industry and service related data. Further, it tries to explore sectoral effects within industry, focusing on manufacturing sector.

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<sup>5</sup> World Economic Outlook, IMF, 2006

<sup>6</sup> *ibid.*

<sup>7</sup> *ibid.*

## AGRICULTURE, INDUSTRY AND SERVICES

While considering the share of value added in these sectors, it is evident that Industry has relatively high share compared to agriculture and service sector. This is especially significant in the case of ASEAN 4 and China. However the value addition is low as against predicted in the case of India. On the other hand share of employment in agriculture is very high across developing Asia and much more than predicted. Only in India we can see growth in service sector standing well ahead of predictions. China and to a lesser extent ASEAN 4 are characterized by an exceptionally high share of value added in Industry and an exceptionally low share in services ,compared to other countries and predicted levels<sup>8</sup>.

Another interesting factor is high share of agriculture [in employment share] in the economies of developing Asia in general, and China and India in particular. At the same time productivity of agriculture is relatively low in the region. But while comparing with other developed countries, Latin America and developing countries, employment share in agriculture is sharply declining in Asia over the years. Within the region, China, ASEAN-4, Korea and Taiwan show strong shift from agriculture to other sectors. For instance agriculture accounted for about a third of Korea's and Taiwan's economy in 1960s but by 1980s it declined to less than one tenth. Across developing Asia, labor mobility is more towards service sector than industry. Interestingly, while in most of Asia share of industry in total employment is still growing, in Japan and the NIEs a movement from industry to services is well underway<sup>9</sup>.

When we analyse the impact of sectoral mobility on aggregate productivity, we have to consider inter sectoral differences in productivity levels. Worldwide the labor productivity in non agriculture is about 3 times higher than agriculture, in Asia this is larger because of the low agricultural productivity rate over the years<sup>10</sup>. This played significant role in Asian economic growth, since low productivity in agriculture encouraged mobility to service sector and industry. This is especially true with regard to China and India where we can see high intersectoral productivity differentials. Hence, we can expect high productivity growth in industry and services across the region as a whole and India and China in particular.

While we consider sector specific growth saga, world wide pattern highlights productivity growth in industry and agriculture than in services. In the case of Asia, three other facts stand out.

Firstly, All over Asia-except India -productivity growth is highest in industry. In India productivity is higher in services mainly because of rapid growth in ICT coupled with trained human capital. Policy interventions including deregulation of services sector, privatization FDI and financial sector reforms enhanced India's performance in service sector.

Secondly, productivity growth in Asia in industry and services far exceeded other regions of the world. Within Asia also, countries with higher productivity growth in one sector tended to have higher productivity growth in other sectors. Hence, it is evident that

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<sup>8</sup> Asian Development Outlook, 2006. Asian Development Bank.

<sup>9</sup> World Economic Outlook, IMF, 2006

<sup>10</sup> World Development Indicators, World Bank, 2006.

country specific factors have significant role in economic productivity and growth in different sectors which in turn affect the aggregate performance of the economy.

Thirdly, in the case of Asia, productivity growth eventually decelerated after initial take off, especially in services, although this process has not yet visible in India and China. In general we can assume that sectoral shift, sectoral composition and intra sectoral productivity growth helped Asian economies to attain a greater growth performance. At the same time Latin America's relative stagnation and divergence from US economy reflect lagging productivity growth with in industry and services.

### **ROLE OF POLICY INTERVENTION**

The above analysis of inter regional and inter sectoral productivity growth pattern highlights the role of policy and institutional mechanisms as chief engine of growth in Asia. Inter-sectoral resource movement also play vital role in this regard. So it is imperative to examine the extend of policy impact on these resource shifts.

Trade openness, institutional quality, financial sector reform favorable business environment infrastructure, well designed education policy etc are some of the factors which determine high productivity growth through human capital formation. Asia's performance in this regard is far ahead of Latin America and other developing countries, especially in terms of institutional quality, trade openness and financial sector development. But here we can see wide regional disparity also. For example the quality of infrastructure is higher in Japan and NIEs compared to other Asian countries. Naturally the productivity ratio is quite high in these economies. Institutional factors determine or facilitate shift from agriculture to non agricultural sectors and thus contributes aggregate productivity growth. Trade openness played important role in encouraging the movement of labor out of agriculture sector in Japan and NIEs and ASEAN-4, where as slow process of opening up of economy in China and India resulted in slow pace of shift. It is thus clear that the institutional policy frame work of trade liberalization has direct impact on sectoral reallocation and become the strong engine of growth. Empirical studies suggest that deregulation and greater integration with world economy would be beneficial for unlocking the sectoral growth potential in Asia. Increasing the transparency and consistency of regulation and streamlining administrative procedure would also be advantageous to Asian economies in long run.

Another area of importance is improving the quality of corporate governance. The region still lags behind advanced economies in terms of corporate governance and the resultant productivity benefits. Looking ahead, the analysis suggests that continued convergence towards advanced economy income and productivity level requires further liberalization and macro economic stability measures ,more investment in education and technology, qualitatively different infrastructure, favorable business climate and political will from institutional leadership to go ahead with the future vision.

## CONCLUSION

Economic growth in most Asian countries has been a story of ups and downs, stability and stagnation. Most of the economies in this region have achieved moderate to rapid growth over medium to short periods of three to ten years, yet maintaining positive growth rates over longer periods. Both income per capita and labour productivity in most sectors have showed convergence towards advanced economies. At the same time, there exist wide gap between rich and poor people, especially in other developing countries. The burning issue here is how to translate the achievement in growth productivity for sustainable economic development based on equity and social justice. Effective social nets, widespread access to education and health care, encouraging entrepreneurship among all sections of population, creation of more employment opportunities in service and industries etc will definitely enhance Asia's chance for a better future, better growth performance and better social equity.

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